

Message Text

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ACTION EA-09

INFO OCT-01 EUR-12 IO-13 ISO-00 AID-05 CIAE-00 COME-00
EB-08 FRB-03 INR-07 NSAE-00 USIA-06 TRSE-00 XMB-02
OPIC-03 SP-02 LAB-04 SIL-01 OMB-01 NSC-05 SS-15
STR-04 CEA-01 L-03 H-01 PA-01 PRS-01 AGRE-00 ITC-01
/109 W

-----161904Z 056561 /15

R 160745Z MAR 77
FM AMEMBASSY TOKYO
TO SECSTATE WASHDC 6173
INFO AMEMBASSY BONN
AMEMBASSY LONDON
AMEMBASSY PARIS
USMISSION OECD PARIS
AMEMBASSY ROME
USMISSION EC BRUSSELS
USMISSION GENEVA
AMEMBASSY OTTAWA

C O N F I D E N T I A L SECTION 1 OF 2 TOKYO 3682

PASS TREASURY, CEA AND FEDERAL RESERVE

E.O. 11652: GDS
TAGS: EGEN JA
SUBJECT: JAPAN SPURS BALKY ECONOMY ON SUMMITS' EVE

1. SUMMARY. ON EVE OF FIRST OF TWO SUMMITS WHICH ARE EX-
PECTED TO FOCUS ATTENTION, INTER ALIA, ON WORLD
ECONOMIC RECOVERY, JAPANESE ARE CONCERNED TO FIND THEIR
ECONOMY IS STILL IN BLAHS. DEMAND IS WEAK, PRODUCTION IS
FLAT AND INFLATION HAS EVEN BEEN ACCELERATING. SERIES OF
EARLIER MEASURES TO DEAL WITH ECONOMIC SLOWDOWN IS IN PLACE
BUT HAS NOT REALLY HAD TIME TO PRODUCE SUBSTANTIAL EFFECTS.
APPROACH OF SUMMITS COMBINED WITH GROWING CONCERNS ABOUT
PRIVATE INVESTMENT OUTLOOK TO PRODUCE ANNOUNCEMENTS OF
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ADDITIONAL EXPANSIONARY ACTIONS ON THREE FRONTS DURING WEEK
OF MARCH 7-11. DIET BUDGET DELIBERATIONS ON MARCH 9
BROUGHT AGREEMENT OF ALL PARTIES TO CUT TAXES BY MORE
THAN \$1 BIL, IN ADDITION TO \$1.5 BIL REDUCTION ORIGINALLY
PROPOSED BY GOJ. BANK OF JAPAN MARCH 11 ANNOUNCED DECISION
TO LOWER ITS DISCOUNT RATE FROM 6.5 PERCENT TO 6.0 PERCENT
EFFECTIVE MARCH 12. FINALLY, CABINET ON MARCH 11 ANNOUNCED

NEW PACKAGE OF ADMINISTRATIVE MEASURES TO STIMULATE ECONOMY. WHETHER GOJ WILL BE ABLE ACHIEVE ITS PROJECTED 1977 REAL GROWTH TARGET OF 6.7 PERCENT REMAINS TO BE SEEN. IT IS EVIDENT, HOWEVER, THAT JAPANESE ARE COMMITTED TO 6.7 PERCENT GOAL AND ARE WORKING HARD TO ACHIEVE IT. ON MARCH 10 FUKUDA SAID FLATLY THAT HE WILL "SEE TO IT" THAT TARGET ACHIEVED. ANY FURTHER STIMULATIVE ACTION DURING NEXT FEW MONTHS, HOWEVER, CAN BE EXPECTED TO FOCUS ON MONETARY POLICY. END SUMMARY.

2. AS GOJ APPROACHES HIGH-LEVEL MEETINGS WITH USG AND OTHER MAJOR INDUSTRIALIZED WESTERN NATIONS, JAPANESE ECONOMY IS STAGNANT THOUGH INFLATIONARY. JAN-MAR 1977 GROWTH WILL HAVE TO IMPROVE MARKEDLY OVER TWO PREVIOUS QUARTERS (ANNUAL RATES OF ONLY 1.4 PERCENT JULY-SEP 1976 AND 2.3 OCT-DEC 1976) EVEN FOR GOJ TO MEET ITS FY 1976 (APRIL 76-MAR 77) REAL GROWTH TARGET OF 5.7 PERCENT.

3. INDICATORS SINCE BEGINNING 1977 ARE HARDLY MORE FAVORABLE. FAR AND AWAY LARGEST CLOUD ON ECONOMIC HORIZON IS OUTLOOK FOR PRIVATE PLANT AND EQUIPMENT INVESTMENT, FOR WHICH LATEST SURVEYS OF INTENTIONS INDICATE SLOW OR EVEN NEGATIVE REAL GROWTH IN YEAR AHEAD. ONE MEASURE OF CONSUMPTION, DEPARTMENT STORE SALES, WAS IN JAN, 10.2 PERCENT OVER YEAR EARLIER BUT WAS PROBABLY NOT RUNNING MUCH IF AT ALL AHEAD OF INFLATION. LATEST REVISED FIGURES SHOW SEASONALLY ADJUSTED INDUSTRIAL OUTPUT DECLINING SLIGHTLY IN JANUARY. BANKRUPTCIES REMAINED HIGH IN JAN AND FEB, BOTH IN NUMBER OF CASES AND IN TOTAL DEBTS.

4. CONCERNS ABOUT THIS SORT OF DEVELOPMENT LED TO THE GOVT'S CONFIDENTIAL

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NOV STIMULUS PACKAGE AND TO FORMULATION OF A SUPPLEMENTARY BUDGET IN DECEMBER 1976. HOWEVER, DIET PASSAGE OF LATTER MEASURE OCCURRED ONLY IN FEB 77, SO IMPLEMENTATION HAS BEEN CONSIDERABLY DELAYED.

5. THE SLUGGISHNESS OF DOMESTIC DEMAND, TOGETHER WITH A PROBABLE DECLINE IN THE RATE OF EXPORT INCREASE DURING FY 77 (AN EXPECTATION DERIVED BOTH FROM WORLD RECOVERY PAUSE AND FROM FOREIGN RESISTANCE TO RAPID JAPANESE EXPORT EXPANSION), ARE NOW FEEDING DOUBTS ABOUT JAPAN'S ACHIEVING THE 6.7 PERCENT FY 77 ECONOMIC GROWTH RATE WHICH GOJ PROJECTED EARLY THIS YEAR. FURTHER, CURRENT ECONOMIC TRENDS THREATEN ACHIEVEMENT OF THE SORT OF GROWTH NEEDED TO ESTABLISH A FIRM SENSE OF RECOVERY IN JAPAN AND A GROWING MARKET FOR THE EXPORTS OF JAPAN'S TRADING PARTNERS DURING REMAINDER OF YEAR.

6. THESE UNFAVORABLE TRENDS, ALONG WITH APPROACH OF SUMMITS, LED GOJ TO TAKE, DURING WEEK OF MARCH 7-11, THREE NEW EXPANSIONARY STEPS. ON MARCH 9 DIET DEBATE OF

FY 77 BUDGET REACHED SETTLEMENT WHEN LIBERAL
DEMOCRATIC PARTY LEADERSHIP ANNOUNCED A COMPROMISE WITH
OPPOSITION PARTY TO REDUCE CENTRAL GOVT INCOME TAXES BY
YEN 653 BIL (ABOUT DOLS 2.3 BIL), A FIGURE ABOUT MIDWAY BETWEEN
YEN 353 BIL (ABOUT \$1.2 BIL) ORIGINALLY PROPOSED BY GOJ
AND YEN 1 TRILLION (ABOUT \$3.5 BIL) ASKED BY OPPOSITION.
IN ADDITION, OPPOSITION INDUCED GOVT TO COUGH UP YEN 63
BIL OF ITS CONTINGENCY FUNDS FOR WELFARE GRANTS. GOJ'S
YEN 79 BIL LOCAL TAX CUT PROPOSAL REMAINED UNCHANGED.
ON MARCH 11, THE BANK OF JAPAN FORMALLY ANNOUNCED A CUT IN
ITS DISCOUNT RATE FROM 6.5 PERCENT TO 6.0 PERCENT, EFFECTIVE
MARCH 12. THIS STEP HAD BEEN PREDICTED WIDELY SINCE BEFORE
THE BEGINNING OF THE YEAR. ALSO ON MARCH 11, THE FUKUDA
CABINET ANNOUNCED A NEW ADMINISTRATIVE PROGRAM OF EXPANSIONARY
MEASURES, INCLUDING SPEEDING UP OF PUBLIC WORKS PROJECTS
AND HOUSING LOAN ALLOCATIONS, ARRANGING FOR EASING OF PRIVATE
CREDIT, AND PROMOTION OF ELECTRIC POWER PLANT INVESTMENT.
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/109 W

-----161903Z 065009 /42

R 160745Z MAR 77
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INFO AMEMBASSY BONN
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USMISSION OECD PARIS
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7. BUDGET COMPROMISE IS OF SPECIAL INTEREST BECAUSE IT WAS ARRIVED AT BY DIET AT INSISTENCE OF OPPOSITION. RATHER THAN (AS HAD BEEN THE CASE TRADITIONALLY) BY PROCESS OF ALMOST ENTIRELY INTRA-GOJ NEGOTIATION WITH POLITICAL GUIDANCE FROM LDP. SPECIAL CIRCUMSTANCES INFLUENCED OUTCOME OF DEBATE, INCLUDING GOJ'S DESIRE BOTH TO REACH EARLY SUBSTANTIVE AGREEMENT ON BUDGET AS PRIME MINISTER PREPARES FOR FOREIGN JOURNEYS AND TO ESTABLISH IMPRESSION OF GOJ EFFECTIVENESS WHICH WOULD HEARTEN BUSINESS WORLD. IN FACT, GOJ HAS NOT YET DECIDED HOW TO FINANCE ADDITIONAL TAX CUTS. NEVERTHELESS, THE INCREASE IN THE TAX CUT (WHICH PRIME MINISTER FUKUDA HAS SUGGESTED MIGHT TAKE THE FORM OF A LUMP-SUM REBATE) IS A SIGN THAT JAPANESE BUDGETARY PROCESS IN FUTURE MAY BE A CONFIDENTIAL

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NEW BALLGAME AND RESULT IN LESS CONSERVATIVE FISCAL POLICIES.

8. THE MARCH 11 FOUR-POINT PROGRAM IS AN ECHO OF THE EXPANSIONARY MEASURES IN THE NOV 76 GOJ PROPOSALS WHICH ALSO FOCUSED HEAVILY ON ACCELERATION OF EXPENDITURE PLANS. YET IN CONJUNCTION WITH DELAY IN IMPLEMENTING FY 76 SUPPLEMENTAL, INTRODUCTION OF NEW PROGRAM IN MARCH MAY MEAN THAT A SUBSTANTIAL PORTION OF ALL THIS PROPOSED SPENDING IS JUST BEGINNING TO WORK ITS WAY INTO THE ECONOMY. IN THIS CONNECTION IT IS INTERESTING TO NOTE A RECENT REPORT OF UNUSUALLY AMBITIOUS NEW ADVERTISING CAMPAIGNS, SUGGESTING THAT SOME BUSINESSMEN AT LEAST ARE MORE OPTIMISTIC ABOUT CONSUMPTION TRENDS.

9. THE LOWERING OF THE BOJ DISCOUNT RATE DOES NOT IN ITSELF APPEAR LIKELY TO GIVE MUCH STIMULUS TO INVESTMENT IN THE CURRENT UNCERTAIN CLIMATE, ALTHOUGH THE EXPECTED REDUCTION IS WELCOMED AS A SIGN THAT JAPANESE FINANCIAL AUTHORITIES ARE AWARE INVESTMENT NEEDS TO BE ENCOURAGED. IN FACT, THERE WILL PROBABLY NOT BE MUCH REDUCTION IN IMPORTANT LENDING RATES HERE UNTIL THERE ARE REDUCTIONS IN IMPORTANT DEPOSIT RATES -- IN PARTICULAR ON SAVINGS DEPOSITS.

10. THE GOJ'S FREEDOM TO TAKE EXPANSIONARY MEASURES CONTINUES TO BE LIMITED BY INFLATION. THE TOKYO CONSUMER PRICE INDEX ROSE AT 12 PERCENT ANNUAL RATE OVER PAST THREE MONTHS, AND FUKUDA HIMSELF HAS NOW VIRTUALLY CONCEDED IMPOSSIBILITY OF ALL JAPAN CPI INCREASES BEING HELD TO TARGET OF 8.6 PERCENT FOR YEAR ENDING MARCH 31, 1977. APPRECIATION OF YEN BY 4 PERCENT IN RELATION TO DOLLAR SINCE END 1976 EASES IMPORT PRICES BUT DEFLATIONARY IMPACT

ON GENERAL PRICE INDICES LIMITED BECAUSE IMPORTS
ABSORB LESS THAN 15 PERCENT OF JAPAN'S NATIONAL INCOME.
POLITICAL SENSITIVITY OF THE INFLATION PROBLEM
PROVIDES A SPECIAL REASON FOR HANDLING IT WITH CARE.
RESULTS OF A KYODO NEWS SERVICE POLL REPORTED IN MARCH 14
TOKYO NEWSPAPERS SHOW CONSUMER PRICES AS UPPER HOUSE
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ELECTION ISSUE OF MOST CONCERN TO RESPONDENTS BY MORE
THAN TWO-TO-ONE MARGIN OVER ANY OTHER SINGLE ISSUE.

11. GIVEN CONSTRAINTS AND UNCERTAINTIES, JAPAN'S POWER OR
TRACTION AS AN ENGINE OF THE WORLD ECONOMY OBVIOUSLY IS NOT
UNLIMITED. YET THE GOJ ACTIONS OF THE LAST WEEK HAVE
PROVIDED THE JAPANESE ECONOMY WITH BOTH PSYCHOLOGICAL STIMULUS
THROUGH THEIR DISPLAY OF WIDE RANGING AND CONCERTED EXPAN-
SIONARY ACTION, AND ECONOMIC STIMULUS THROUGH THE CONCENTRATION
OF PUBLIC SPENDING WHICH MAY BE EXPECTED DURING THE NEXT
FEW MONTHS. IN THE LONGER RUN, WHETHER JAPAN CAN MEET
ITS FY 1977 GROWTH TARGET DEPENDS LARGELY ON THE
RESPONSE OF THE PRIVATE SECTOR, AND MORE PARTICULARLY OF
PRIVATE DOMESTIC INVESTMENT, TO THESE STIMULI. IT
APPEARS THAT THE GOJ, PLEDGED TO A PROGRAM OF EXPANDING
PUBLIC INVESTMENT AND PRESSED BY EXPANSION-MINDED (OR AT
LEASE CONCESSION-HUNGRY) BUSINESSMEN ON ONE HAND AND A
CONSUMER-ORIENTED OPPOSITION ON THE OTHER, WILL CONTINUE
TO STRIVE TO LEAD JAPAN TO THE REQUISITE INVESTMENT AND
CONSUMPTION LEVELS. AS THE PRIME MINISTER HIMSELF SAID
AT THE FOREIGN CORRESPONDENTS' CLUB MARCH 10 (PERHAPS
SOMEWHAT RASHLY) HE WILL "SEE TO IT" THAT JAPAN'S GROWTH
TARGET IN YEAR AHEAD IS REALIZED, ADDING THAT GOJ WOULD
BE PROMPT AND FLEXIBLE IN TAKING COUNTERMEASURES SHOULD
BOTTLENECKS EMERGE. HOWEVER, WITH THE BUDGET AGREED,
AND BARRING MAJOR CHANGES IN CIRCUMSTANCES, ANY FURTHER
STIMULATIVE ACTION IN THE MONTHS IMMEDIATELY AHEAD MAY
BE EXPECTED TO FOCUS ON MONETARY POLICY, WITH CONSEQUENT
POSSIBLE DOWNWARD PRESSURES ON YEN RATE.
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Message Attributes

Automatic Decaptioning: X
Capture Date: 01-Jan-1994 12:00:00 am
Channel Indicators: n/a
Current Classification: UNCLASSIFIED
Concepts: REPORTS, ECONOMIC CONDITIONS
Control Number: n/a
Copy: SINGLE
Sent Date: 16-Mar-1977 12:00:00 am
Decaption Date: 01-Jan-1960 12:00:00 am
Decaption Note:
Disposition Action: RELEASED
Disposition Approved on Date:
Disposition Case Number: n/a
Disposition Comment: 25 YEAR REVIEW
Disposition Date: 22 May 2009
Disposition Event:
Disposition History: n/a
Disposition Reason:
Disposition Remarks:
Document Number: 1977TOKYO03682
Document Source: CORE
Document Unique ID: 00
Drafter: n/a
Enclosure: n/a
Executive Order: GS
Errors: N/A
Expiration:
Film Number: D770090-0635
Format: TEL
From: TOKYO
Handling Restrictions: n/a
Image Path:
ISecure: 1
Legacy Key: link1977/newtext/t19770353/aaaabuxa.tel
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Litigation History:
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Office: ACTION EA
Original Classification: CONFIDENTIAL
Original Handling Restrictions: n/a
Original Previous Classification: n/a
Original Previous Handling Restrictions: n/a
Page Count: 5
Previous Channel Indicators: n/a
Previous Classification: CONFIDENTIAL
Previous Handling Restrictions: n/a
Reference: n/a
Retention: 0
Review Action: RELEASED, APPROVED
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Review Release Date: n/a
Review Release Event: n/a
Review Transfer Date:
Review Withdrawn Fields: n/a
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Status: NATIVE
Subject: JAPAN SPURS BALKY ECONOMY ON SUMMITS' EVE
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To: STATE
Type: TE
vdkgvwkey: odbc://SAS/SAS.dbo.SAS_Docs/99cd09b7-c288-dd11-92da-001cc4696bcc
Review Markings:
Margaret P. Grafeld
Declassified/Released
US Department of State
EO Systematic Review
22 May 2009
Markings: Margaret P. Grafeld Declassified/Released US Department of State EO Systematic Review 22 May 2009